

Sept. 30, 1992

LETTER 1105

**THE MARKET:** The Dow has been locked into a 7.5% range all year. It's a stand-off -- a case of overvaluation, a rotten economy -- but low, low interest rates. Merrill Lynch notes that from highs set during the first four months of 1992 to their lows set in the second four months, 54% of all US stocks were down 20% or more. Some analysts feel that this kind of broad corrective action is all that's needed to strengthen the market's internal position. I don't agree. I look at the above statistic as simply a case of market deterioration.

*The Primary Trend* report (700 N. Water St., Milwaukee, WI 53202) notes that the S&P Brokerage Stocks Group has topped out (it's down 22% from its high). Top-outs in the brokerage group have had an excellent record of preceding tops in the general market. And there's an obvious rationale for this. If there's a major correction or bear market coming up, earnings for the brokers are due to decline. Stock brokers make money on volume, but bear markets mean losses, lost customers and lower volume. Cynical observation: did you ever see a branch manager in a brokerage firm ask a salesman, "Charlie, are your customers making money?" Hardly; he'll ask, "Charlie, how are your sales this month?"

As for me, I still don't have anything in the price action to tell me it's a bear market. Personally, as subscribers well know, I don't care for this market. I think it's over-priced, and I think the bull is very long in the tooth. But as I've said repeatedly, I want the Dow to break below 3181.35 before I can say that a bear market is in force. And I also want my Primary Trend Index to break below its 89-day moving average before I say that a bear market is in force. So far, neither event has occurred. To summarize -- I don't like the market, I don't like Bush, I don't like Clinton, and finally I don't like what I see coming up (see later section of this Letter). Boy, am I a grouch.

One more item (you're not going to like this): I believe the bond market has topped out. Whether the top-out is based on better US housing starts, hopes of a general economic revival or something else I don't know. Of course the top-out may also be based on the disastrous state of US (deficit) finances. For whatever reason, the long-bond chart looks lousy. I think the big bond-ride is over.

**SURPRISES, OPINIONS:** (1) If nothing else, 1992 is the year in which the markets (read Forex or foreign exchange traders) took over from the politicians. We saw the pound sterling collapse and pull out of the ERM, despite the vows and promises of Britain's leaders. We saw the Italian lira devalued and pull out of the ERM. We saw the French upping their interest rates to defend the franc. We saw Spain devalue.

The Forex traders knocked off one currency after another, always going after the weakest currency. How did they do it? For one thing, the Forex traders have far more money than the central banks. And they are well aware of the banks' weaknesses (the central banks had to keep their currencies within the ERM band). That left the central banks in the position of trying to defend positions that were basically indefensible -- unless, of course, they were willing to raise interest rates (which France did on Sept. 23).

(2) Frightened international money poured into the dollar prior to the French vote on Maastricht. Why? The dollar was the only item big enough to handle the amount of switching that was to be done by frightened investors.

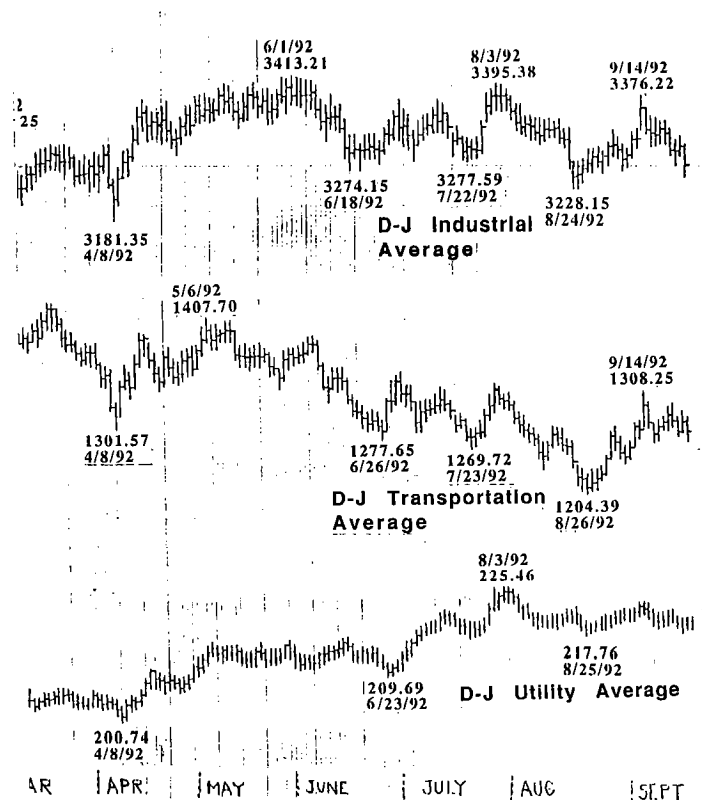
Sept. 18 DJIA 3327.05; PTI 3569; A-D Ratio -9.44  
Sept. 25 DJIA 3250.32; PTI 3559; A-D Ratio -10.07  
Dow Yield: 3.19%; Dow Price/Earnings: 56.3  
Dow 200-day MA: 3283; Dow 30-day MA: 3278  
Dow Times Book Value: 2.49; PTI 89-day MA: 3527  
Percentage of Undervalued Blue-chips: 9%

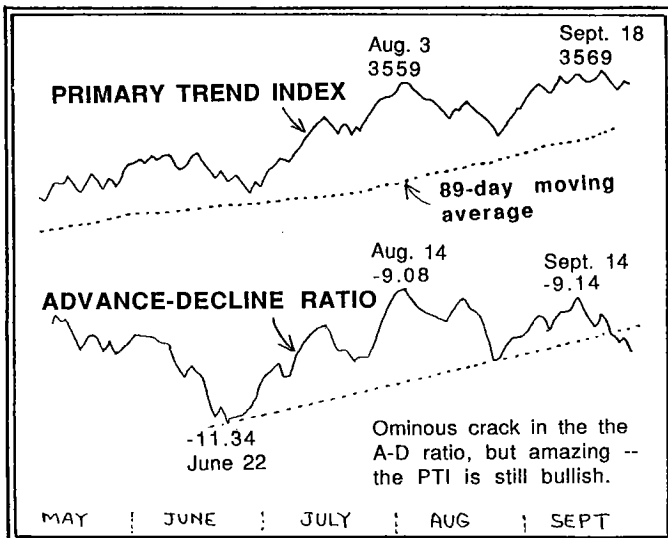
(3) The very close French vote in favor of Maastricht presented as many problems as it "solved." Actually, for all intents and purposes, the vote was even. Being that close, it means that an European union (particularly a single-currency union) is somewhere far off into the future.

Russell thought: I find it almost impossible to believe that the Germans would give up their beloved, hard-currency mark for a European currency. Would the Germans vote in favor of Maastricht? I doubt it. Headline from one German newspaper, "You Beautiful, Strong Mark." From another headline, "Hands Off Our Mark."

(4) The big immediate question on my mind is the dollar/mark relationship. Can dollar strength continue? Would dollar strength continue if Clinton is elected? I'm doubtful on both counts. The difference, as I see it, is (A) a Bundesbank which is hard-nosed, fiercely independent and bound by German law to be anti-inflationary, pitted against (B) a Fed which bends to political pressure, a Fed which is trying to re-inflate, a Fed which has pushed interest rates down to their lowest level in three decades.

**THE PICTURE:** The question on everyone's mind is this -- has the high-priced US stock market been forecasting better times ahead, or has the stock market simply been trading off three years





of declining, Fed-manipulated interest rates? Normally, I would say that aside from the major plus of declining rates, the stock market has been also forecasting better times ahead.

But I must admit to doubts. First of all, the broad M-4 money supply (termed "liquidity") is still virtually standing still, and where there is little or no growth in the money supply, there tends to be no growth in the economy. Next, Ed Hyman of *ISI* counts a total of 84 corporate lay-offs since July against 80 in the same period last year. In other words, the long, seemingly unending string of lay-offs continues, and that's hardly conducive to a rising economy. Next, Hyman notes that on a year-to-year basis, the economies of every G-7 nation, except the US, are in decline. There is a 70% correlation between G-6 industrial production and US industrial production. Industrial production was down in July and so were factory working hours. Furthermore, with all of Europe in recession, US imports were hit and our trade deficit jumped to a 20-month high. Industrial production in August dropped 0.6% from July and factory capacity usage also declined.

Finally (this from the *WSJ*, Sept. 14), "Small business has fallen into its worst slump since the recession, casting an unexpected shadow over the US economic recovery and threatening to undermine small business support for the re-election of President Bush." The latest American Express survey states that demand for goods and services for small business fell in the second quarter at an annual rate of 3.4%. Considering that small business employs two-thirds of America's workers, this is hardly a good omen.

So the question remains on my mind -- Is this market telling us that better times lie ahead? Or have we been witnessing a strange, confused, bear-market type rally, a rally which saw the NYSE Composite and the S&P 500 rally to new record highs, but a rally that (strangely) failed to see new highs in either the Dow or the Transportation Average?

**INVESTMENT POSITION:** I don't have any perfect answers for what's coming up. I don't have the final answer on how to protect ourselves from a government that is moving us steadily towards national bankruptcy.



Yeah, the bull is still in the box, and yes, I haven't any bear market signals. But I'm worried, and I'm particularly worried because I don't have THE answer. The best I can do is this -- play the short-term if you want (I guess we all do it), but I'm thinking of the longer term. And for the longer term I think you have to have some form of D-mark (I chose the German bonds), and I think you have to have some form of gold.

We had the party (1980s), and we spent the money, and we heard the big lies ("everything's all right"). Pretty soon we're going to have to deal with the reality. I think reality will be a big bear market, and I go back to something I said in 1974, "In a primary bear market, it's the person who loses the least who is the winner." In other words, everyone loses in a bear market, but well -- the main thing is, you just try to survive. This is particularly true when the currency, the base of all your investments, is in danger.

So I'd just try to get on the liquid side now. D-mark long-bonds, some gold, some dollar items (T-bills, money market funds, etc.), and let's wait patiently. Don't do anything exciting or brilliant here -- if you do, you'll probably end up losing.

Observation: Looking over the 30 Dow Industrials, it's significant how many are well off their highs. Only Amer. Tel., Exxon, GE, MMM, and Philip Morris are near their highs. Amer. Express, Beth Steel, Boeing, GM, IBM, Unit. Technologies and Westinghouse have been taking beatings. The rest are at various stages of correction. This is one tough market, and I suspect only the liars (and Forex traders) have been making money.

**THE ALARM BUTTON:** Do you know how the US federal budget is financed? Check this out! Individual taxes bring in 33% of the money. Corporate taxes bring in 7%. Social Security and Medicare bring in a whopping 30%. Excise taxes and other fees bring in 7%. And the Treasury **BORROWS** the other 23%. It's a study in fiscal insanity.

In other words, the US gets 53% of funds to run the nation as follows: 30% they grab from Social Security and Medicare trusts, and they go out and borrow the other 23%! Are you kidding me? It's unbelievable. Yet nobody seems to notice. Subscribers, we have built a towering house of cards, and neither Bush nor Clinton is talking about it.

All financial flim-flammy must eventually show up somewhere. Where will the US financial horror story begin to show up? The politicians won't talk about it, but the markets will. I believe it will show up both in the dollar and in gold. And certainly in the stock market. But when? Read on.

**JUST DO IT, PLEASE!** In the 34 years that I've been writing these Letters, I've never put forth this kind of request -- actually, I would like to call it a command. I want every one of my subscribers to buy a new book entitled, "**Bankruptcy, 1995, The Coming Collapse of America and How to Stop It,**" by Harry E. Figgie, Jr. and Gerald J. Swanson, published by Little, Brown. Figgie is CEO of billion dollar Figgie International, Inc. (a Fortune 500 company), and he was co-chair of the Grace Commission.

Many of the projections and charts in this book were prepared by Data Resources, Inc. for the *President's Private Sector Survey on Cost Control*, better known as the Grace Commission. As you may or may not know, the Grace Commission (commissioned by Reagan in 1982) told the true story of the disastrous path the US is treading. It's a frightening story that's been ignored (you might say stifled) by Reagan himself, and by all subsequent presidents and all candidates up to the present. To put it bluntly, the report has been shelved.

So far, all the projections of the Grace Commission (since 1985) have been on the button. The page 3 chart shows the incredible deficit story, from Lyndon Johnson, who opted for both guns (Vietnam) and butter, and who then hid the expenses. After Johnson the picture deteriorates further, and the Grace Commission projects the budget-horror that lies in store for us through 1993 to 1996.

What can we expect in the future? Writes Figgie, "By 1995, even if American politicians haven't acknowledged it yet, the rest of the world will have figured out that the US is going to default on its debt. That's when and why our country and lives will come apart."

Of course, this is what I've been saying for years. Our spendthrift, incompetent, self-serving politicians have pushed America steadily towards the brink of bankruptcy. The big question is timing, and that's one of the reasons why I insist that you buy and read this book.

As you know, I've been warning that with the path the US is on, there are only two alternatives, "Inflate or die" (substitute depression and bankruptcy for "die"). This book agrees. It sees us moving to the point where the rest of the world will refuse to accept dollar debt, and, in fact, they will be dumping dollar-denominated debt. At that point, the panic and deflation/depression will be on.

There is an alternative. The alternative will be the time when a desperate Fed is forced to buy up all US debt. At that point the US will move into inflation with rising interest rates and then to hyperinflation. Figgie puts the alternatives in slightly different language. In the book he refers to the two alternatives as "Death by Hyperinflation" or "Death by panic."

Now remember this -- I'm not recommending some wide-eyed crazy gloom-and-doom book. This is a book based on valid projections. It's a book written by two very intelligent men. It's a book that subscribers must read if they want to prepare for events that I am convinced are coming up.

But here's the problem. There are no painless solutions to the deficit dilemma. The book's answer to the situation is to put pressure on Washington to cut spending (with no raising of taxes). And that's fine, except that slicing spending by the required amount would, I believe, throw America's economy from recession into depression. Furthermore, I don't believe any of today's politicians are ready to order the necessary spending cuts. They just won't do it. Let's face it -- all the pressure today is on our politicians to spend more.

I would guess that a national sales tax might be proposed, and even a rise in the gasoline tax. But both of those avenues would be highly deflationary, and that would just heighten the pain.

On September 15 Ross Perot announced that if neither candidate was willing to address the budget deficits, he, Perot, might run for president again. Don't laugh. If Perot throws his hat in the ring again, the threat is that he would capture a lot of Bush votes and swing the election to Clinton (Perot hates Bush). It may be an idle threat on Perot's part, but I wouldn't dismiss it. However, and this is ironic, because Perot quit the race, I don't think people will take what he says seriously. He will be pooh-poohed by the press (they are already ridiculing him). Perot himself, and his actions, may be stupid or absurd, but he does see the deficit crisis correctly. But as I say, I don't think people will take him seriously.

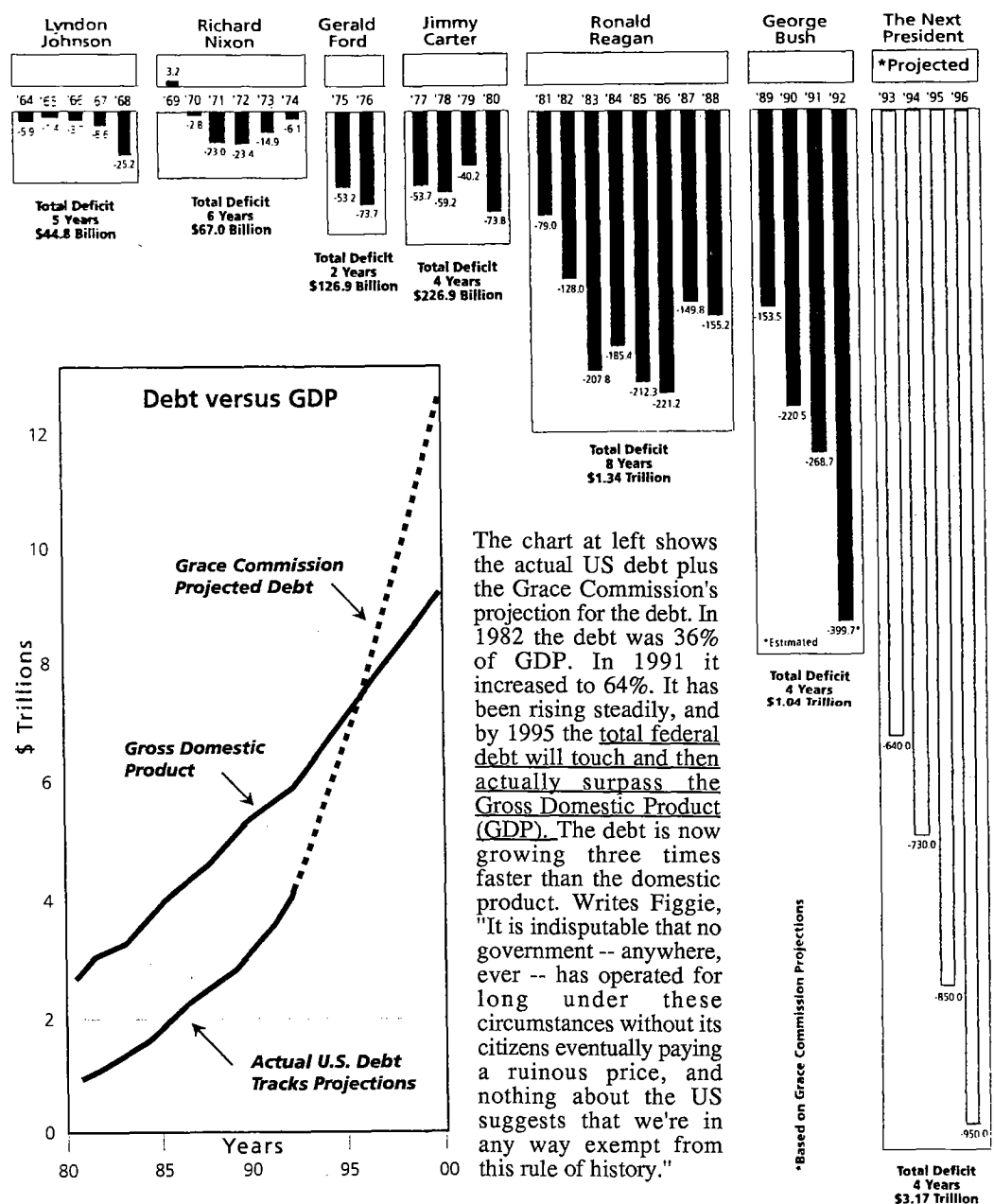
Question: If the projections in this book are correct and the dollar is doomed, what do we do about it? What happens if no one wants dollars, where do they go? After considerable thinking on the subject (to be honest, I've been thinking about this for a long time) I would say that investors will have to go to the strongest currency and to gold (gold being the only real money).

As things stand now, I have to believe that the strongest currency will be the German mark, and I think you will see more and more investors at least hedging by buying German bonds (bunds) or some form of the D-mark.

As for gold, this is real money, and it's the only money that doesn't represent someone else's liability. Thus, at some point I believe we will see a major bull market in gold as an increasing number of investors opt for the safety of the foundation of the monetary pyramid -- gold.

I was describing this whole monetary/budgetary situation over the phone to a friend of mine, and he said, "I'm sorry, I just can't buy it, it's too crazy; it's just too doomy-gloomy."

## FEDERAL BUDGET DEFICITS SINCE 1964 (In Billions of Dollars by Fiscal Years).



I answered, "Listen, at this point it's boiling down to a matter of mathematics and chart projections. You know, back in the '60s I had a Swiss subscriber, and he told me a story I'll never forget. He said, 'Richard, one day I was looking out the window of my New York apartment, looking out over the Hudson River. I noticed two large ships heading towards each other, and I said to myself, "This is too ridiculous, but if these boats stay on that path they're going to crash -- and that can't happen. But do you know, those two ships continued on that same path -- and they crashed!'"

Question: Russell, why do you think that ultimately the mark will be the strongest currency? Why, for instance, will the mark be stronger than the dollar?

Answer: My reasoning is simple and straight-forward. The German economy is subject to a stern discipline in the form of the fiercely independent Bundesbank. On the other hand, the American economy is really undisciplined. Spending is out of control, and the only discipline is in the monetary area via the Fed. The Fed, unfortunately, is subject to political pressure, and it has acted that way. Finally, Americans, unlike the Germans, have little fear of inflation. In America, when the going gets rough, Congress and the Fed opt for inflation.

**NOTES & QUOTES:** The Russian ruble has collapsed. Worth 32 to the dollar, the ruble crashed last week to 241 to the dollar. The Russians have plenty of gold, and I said at the onset that they should make the ruble convertible into gold and produce a real, viable currency. Why the devil they didn't I don't know, but they didn't. Of course, they had US advisors for their currency (always a disaster), and now the ruble is literally worthless. A tragedy that could have been averted. Stupidity reigns.

How big are the various world economies? Roughly, the total world output (Gross Domestic Product) is around \$20 trillion. The US has by far the biggest economy at \$5.445 trillion or about 27% of the whole. Next is Japan with a \$3.140 trillion GDP. Germany is third at \$1.411 trillion. France has a \$1.099 GDP, Italy at \$970 billion, UK at \$923 billion, Canada at \$542 billion and Spain at \$429 billion.

Thus it's clear that the US is the "big dog," the monster economy that has the major swing-power one way or the other. The US is by far the world's biggest buyer of goods. If the US booms, the rest of the world tends to do well (selling its goods to the US). If the US slumps, the rest of the world tends to sink too (as their exports slide). Right now the US is pulling back on buying, and therefore world trade is being squeezed. The trillion dollar question -- will the US pull out of recession, or will it continue to slumber or slide? The answer, I think, should emerge within the next six months.

The London *Economist* took an average of six pollsters' results on the US election and came up with these figures: Clinton 50.2%, Bush 40.8%. Then they make a few observations such as "'Skidmarks of the Week' -- Dan Quayle's attempts to convince everyone that 'family values' was not a code for gay bashing." And "Unpleasant Sights of the Week (and most weeks): Bill Clinton jogging."

It looks as though California (with a 10.5% unemployment rate and a crumbling economy) is definitely in the Clinton camp. As Richard Nixon put it, California is "definitely a lost cause."

I consider *Salomon's* man in Washington, Steve Bell, one of the best and smartest of the political observers (you can see him on CNN). He says that he now counts 294 electoral votes for Clinton (Clinton needs 270 votes to win). Russell opinion: As things now stand, it looks as if Clinton is the winner. But in the silence of the voting booth, with the thought of Clinton's higher taxes and big spending plans -- who knows what the voter will do?

From our "For Shame Dept.": Over the past 12 years neither Reagan nor Bush has even proposed to Congress a budget with

less than a \$60 billion deficit (of course, in retrospect, \$60 billion would have been a bargain).

This from David M. Jones, chief economist at *Aubrey G. Lanston & Co., Inc.*: "If Bill Clinton is elected, I think he will be a huge spender; a Roosevelt-type spender. He's going to come out of the starting blocks running (with large spending programs). It's going back to the old-fashioned Roosevelt stimulus model." Russell comment: And unlike George Bush, Clinton won't have Congress fighting him on his program.

The US debt now stands at \$4.5 trillion. On top of that there are \$8.7 trillion in private debts plus \$1.1 trillion in state and local government debts. That's a grand total of \$14.3 trillion of debt. The interest payments on this ocean of debt now amounts to about \$1 trillion a year.

Some of the US debt is held by foreigners. Actually, the amount of the US national debt held by both foreign private sources and foreign governments is now \$468 billion or roughly half a trillion dollars.

It's obvious that the one thing this massive amount of debt cannot deal with is true deflation. If deflation hits it will make payments on all debts more difficult (dollars will become worth more). This is one reason why central banks (exception, Germany) are now trying to re-inflate. Inflation makes debt more manageable. Last week even Switzerland cut its interest rate.

Of the US government's four trillion dollars in debt, roughly one trillion of that is held by government trusts. The largest portion, \$320 billion, is held by the Social Security trust in special non-transferable government IOUs. Good luck, all you future Social Security hopefuls. When are Americans going to realize that SS is simply a transfer tax, transferring the earnings of the current working generation to the older generation. And how long will working Americans put up with this?

What exactly do Bush and Clinton stand for? According to the *NY Times*, "Bush wants the Government basically to leave the free market alone. Clinton believes the Government should take an active role in directing the nation's economy. Bush believes wealthy Americans are taxed too much. Clinton would raise their taxes. Bush would cut social programs and public works to the bone. Clinton would expand Government spending in many areas and would invest in capital projects like roads and bridges, transportation systems and communication networks. Bush would loosen and abolish Government rules and restraints on business. Clinton wants new regulations on business to protect the environment and to force energy conservation. Bush's ideas about medical care and job training are based on tax incentives. Clinton would require employers to provide medical insurance and training to their employees or pay money to the Government to do the job for them. Bush favors free trade at almost all costs. Clinton is increasingly taking the view that the US should be tougher on its trading partners."

Here are a few interesting quotes from Jeffrey Garten, an investment banker in the Blackstone Group (author of "A Cold Peace: America, Japan and Germany and the Struggle for Supremacy"): "No one is going to listen to Washington as long as it's on a course that the rest of the world considers irresponsible and insane . . . The theology in government that a gradually declining dollar is good for US competitiveness is a dangerous over-simplification." He adds that using a cheap exchange rate to enhance competitiveness is a strategy used by developing countries that sell commodities. These commodities, identical to commodities sold by other countries, can only compete on price -- usually on the low price of labor. But developed countries are expected to compete on quality, such as Japanese autos or German machine tools or American airplanes, making higher wages possible. Exchange rates should not matter so much.

Says Garten, "There is a divergence between the kind of economy we say we want and the Bush administration's benign neglect of the dollar. The weak dollar policy is saying that our vision of the economy is low-wage, commodity intensive. There is no precedent

in history where a major industrial power has been competitive while its currency is depreciating."

In a rundown of the 50 states, *US News & World Report* describes the financial condition of California as "crumbling." Ominously, it also refers to California as the "bellwether" state. In its annual report, *Ernst & Young* states that nearly half of San Diego's biomedical companies and 20% of local biotech firms are considering leaving California. High taxes and bad business environment were listed as the main reasons.

Here's what the UCLA Business Forecasting Project has just announced regarding the bellwether state of California. They say it's in the worst slump since the '30s and that the jobless figure here will top 11% by 1993. The project adds that the California slump has now surpassed the worst of the Texas slump. "The state is now caught in a vicious cycle, with job losses in key sectors constraining income growth and spending, causing cutbacks in production and more layoffs." The report continues, "The cycle has been exacerbated by the downturn in defense spending, falling real estate prices, an unprecedented series of natural disasters -- drought, earthquakes, fires, freezes, floods -- and most recently the Los Angeles riots. Rebounds in neither California housing, local consumer spending, nor the US economy appear imminent." Russell comment: At least they don't mince words.

It's strange, when California was booming they called it "the bellwether state." Now that California is slumping, nobody wants to call it the bellwether any longer. But I wonder -- could it still be the bellwether? Charlie Allmon (*Growth Stock Outlook*, Box 15381, Chevy Chase, MD 20825) notes that California banks hold 74% of the West's \$466 billion in bank assets. While the rest of the West is not doing badly, California has big troubles. In 1991 non-performing assets in the Cal banks were a fat 5.1% (a jump of 52% over 1990) while in the rest of the nation they were 2.0%. For this reason, Allmon believes we could see "a rash of bank failures" in late 1992 and '93.

Is Taiwan the strongest nation, economically, in the world? I've talked about Taiwan in the past, and the answer to the above question should be a yes. Taiwan, a nation of 21 million hard-working people, has the world's highest monetary reserves -- \$80 billion in foreign exchange and bank deposits of over \$300 billion. On top of that Taiwan has a huge store of gold. Over the last ten years Taiwan's GDP growth has averaged over 7%; its gross domestic savings as a percentage of GDP is a huge 28%. Actually, Singapore has the highest savings rate (45%) and the second highest growth rate (7.9%). Of course, what these figures really show is the industry and savings proclivities of the Chinese people. Or as I often put it to a doubting friend, "Have you ever seen or heard of a Chinese restaurant going broke?"

I can't believe it! After lecturing in the last Letter about the spelling of the US Marshals Service, three proof readers and your editor MISPELLED IT. OK, it has one L and "Marshals" is plural, not possessive. It's, blast it, the US Marshals service. I defy 99 out of 100 people to get it right.

Despite the high prices in Europe (due to the dollar's decline), a French hotel chain called Formule 1 charges \$30 a night for one to three occupants. The chain is run by Groupe Actor, the same outfit that runs Motel 6 in the US. Formule now has 230 hotels in France, and it's expanding into Belgium, UK, Holland and Germany.

China continues to boom, and I see it as the "wild card" in the world economy. Investors are pouring money into Hong Kong and Southern China. Thesis: combine the expertise, manufacturing skill and capital of Hong Kong with a 1.2 billion market of hard-working, low-cost Chinese, and you've got a potential economic colossus to contend with. On top of that, the Chinese are great businessmen, and the Chinese population is noted for savings (reputedly, Chinese savings rate is 25% to 35%). Note: the Chinese trade surplus with the US is now \$15 billion and rising.

In the US 60% of all adults have credit cards. Total consumer credit is now \$182 billion -- in 1972 it was \$3.9 billion. Another US credit balloon -- home credit. From \$10 billion in 1985 home-credit lines have exploded to \$120 billion today. No wonder consumers are trying to pare down debt. Comparison: in Germany only 1% of the population owns credit cards. German consumers have a natural aversion to debt. German savings rate: 13.9%.

The German Bundesbank was modeled after the US' Fed. By law the Bundesbank must support the government's economic policy. Founded in 1957, the bank is known for its independence. In fact, it is situated outside the capital, in Frankfurt, as a symbol of its independence from the capital's politicians. The Bundesbank employs 17,000 people. Its obsession is keeping inflation out of Germany. The strength and prestige of the mighty D-mark is a point of national pride with every German, and to them the Bundesbank can do no wrong.

The head of the Bundesbank is Helmut Schlesinger, known to be dogmatic, a longtime observer and highly cerebral. Schlesinger's tenure as head of the bank will be brief, only two years left. But he is there at a crucial time for Germany and the banks.

Currency Markets: Unlike the NYSE, where there is a visitor's gallery, much publicity and 2,800 dealers and exchange employees, the currency markets are relatively unknown to investors. There is no one place where currency traders do their business. Trading is conducted via a web of computer screens, telephone lines and brokers' boxes which link intermediaries, whose jobs are to match buyers and sellers. About 80% of the \$100 billion and more currency trading in the US is done by the banks. Some of the biggest bank profits come from currency (and option) trading. Chase Manhattan in NYC has 50 traders and salespeople, Harris Trust trades around the clock with 22 dealers. The new Globex market now trades major currencies all night long. Here in California, currency trading halts at midday, then starts again at 4PM in the afternoon and continues (Globex) until four in the morning. Then it starts again at 5:15AM.

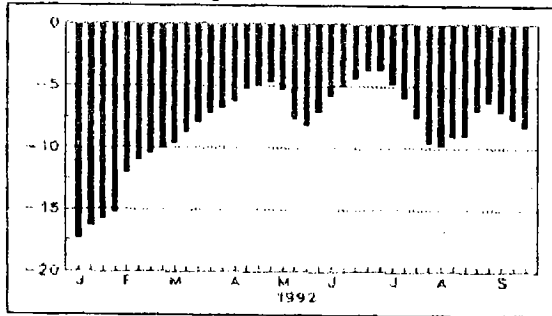
I put up a satellite which gives us the quotes around the clock. And yes, I trade currency options -- I sell them, never buy them. But I don't recommend the procedure to subscribers, it's highly technical. One advantage for me in selling currency options, it keeps me in close touch with what's happening overseas. And as you know, A LOT has been happening in the new global world.

Did you ever order anything from fine old very reputable L. L. Bean Company out of Maine? I just received a pair of moccasins -- darn well made and a real bargain at \$39.50. Send for their fine catalogue: (800) 221-4221; you won't be sorry (PS: Anytime I recommend anything in these Letters, rest assured I don't make a cent on it. I recommend items occasionally, only because I like those items).

Here's something that is guaranteed to shake up "family values." Madonna (remember her) is coming out, October 21, with her new book which is simply entitled, *Sex*. Warner Books has ordered a giant first printing of 835,000 copies, the largest initial release of any illustrated book in history. The book is reputedly a mass of chains, whips, knives, lesbians, skinheads, frotage, you name it (if you can). The book will be priced at a whopping \$49.95. It will be 128 pages, printed in five colors, spiral bound and the covers will be aluminum (81,036 photos were taken before final selections were made, and 750,000 pounds of aluminum were ordered for binding). The books will be published in six languages. Russell Comment: Expect a massive blitz-hype for the book; it won't be easy to sell a 128-page volume for \$49.95.

I just received by FAX *Sindlinger's* latest comments on the economy. He says the unemployment rate rose to 10.5%. *Sindlinger's* reports Household Money Supply fell to 28.8%, only one-half percentage point above the recession low recorded on July 25. His Current Income Index for families dropped to 49.0%, just 1.2% above its record low of only five weeks ago. Finally, his Consumer Spending Indicators have also turned down (see chart). All in all, not a happy report for Mr. Bush or the economy.

CONSUMER SPENDING INDICATORS  
Among All U.S. Consumers



**GOLD, THE DOLLAR AND VALUES:** If there is one rule that fits all investing it is this -- "Ultimately, value will out." In other words, the true value of every investment will ultimately be expressed by the markets.

Now consider this from my tall friend, Jim Grant and his recent report (*Grant's Interest Rate Observer*, 30 Wall Street, NYC 10005): "What does the world see in an oval portrait of Andrew Jackson or Benjamin Franklin? Not a yield, of course, nor any intrinsic value. The cost of producing a bill is 3.9 cents, and the Bureau of Engraving and Printing keeps three shifts a day working seven days a week to satisfy the growing demand. The Bureau's new, web-fed intaglio currency press, which delivered its first crisp bills only last June, promises even greater efficiency ('The web-roll-to-sheets system delivers 10,000 sheets in about 35 minutes,' a press release says, 'as compared to 8,000 sheets per hour for the sheets-fed presses.' A spokesperson's call is, simply, 'something to behold.')."

All right, so the US government is speed-printing paper (actually, they're not paper, they're cotton and linen) dollars -- denominations of ones, fives, tens, fifties, hundreds -- printing them 24 hours a day seven days a week at the rate of 20,000 sheets an hour.

Now consider this: the government prints four one hundred dollar bills, and the cost to Uncle Sam of printing those four bills is **15.6 cents**. Then you can take that 15.6 cents worth of cotton and linen and buy about an ounce and a quarter of gold. It costs the mines, on average, about \$280 to produce a single ounce of gold.

So something is crazy. The US government is in the "publishing business," and what the government publishes on its high-speed printing presses is "money." That so-called money (it has absolutely no intrinsic value) can buy precious metal at a total cost of only 15.6 cents, less than a lousy silver-less quarter.

Furthermore, the US government is running deficits of \$1.15 billion dollars a day, and the Treasury is covering at least part of those deficits with printing-press, no-intrinsic-value "money."

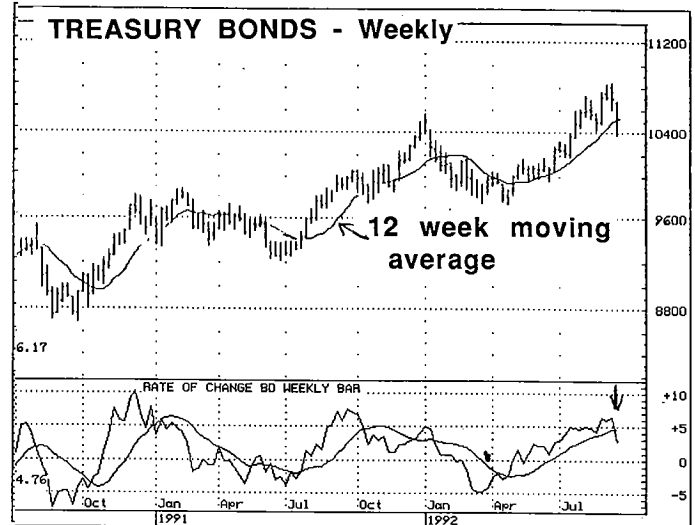
So you know something is wildly wrong. What's wrong is that the world is saying that 350 dollars worth of fiat (paper) money is equal in value to an ounce of gold -- gold that it takes capital and the sweat of men's brows to get out of the ground.

Here's my conclusion: The US public and the rest of the world for that matter, are being sold a phoney bill of goods when they hold dollars over any considerable period of time. Dollars are of no intrinsic value, and are only accepted as a medium of exchange because people still have confidence in the morality and discipline of the US government.

But from the other side, gold is far too cheap. If you can buy an ounce of gold for what it costs the US government 15.6 cents to manufacture, then you can count on it -- in the end the value of gold will out. Gold is real money, it has intrinsic value, it has a 5,000 year history of being accepted as something of value.

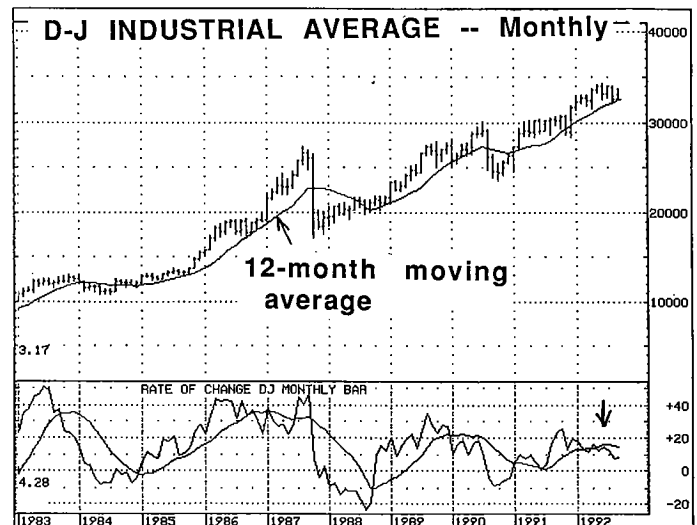
On the other hand, the dollar is the currency of a government that flagrantly mismanages its financial affairs, a government that is running up the greatest mountain of debts in history. Gold's time is coming. Values will out.

**LATE NOTES:** All right, so I'm a grouch and a kill-joy. But I want to show you a couple of charts that bother me. The first is a weekly chart of the **T-bonds** with a 12-week moving average running through the price action. On the lower panel of this chart I have included momentum in the form of a 12-week rate-of-change (price divided by the price 12 weeks ago), and a 12-week moving average (smoother line) of the rate-of-change. Note that the momentum line has just plunged below its moving average. In the past this has NOT been a good sign for the bonds. The bearish crossing tends to have a lead time, but it does suggest to me that the bonds could be toping out.



The second chart is a monthly chart of the **Dow**, and running through the price is a 12-month moving average. The lower panel of this chart shows momentum in the form of a 12-month rate-of-change along with a 12-month moving average (smoother line) of the rate-of-change. Here again, we see the momentum line sinking below the moving average line. In the past when this has happened it's been a signal for trouble coming up in the market. Note that each momentum peak -- 1987, 1989, 1991 -- has been lower than the preceding, not a good sign.

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Weakness. Europe is in recession, and its stock markets are very weak, the dollar remains weak, and the US economy remains weak -- what's next? Maybe another discount rate cut. Perot's still the big, kooky enigma. Bush and Clinton are both weak and "iffy" (which is why they're even bothering to meet with Perot).